



Agenda Item 3b

November 15, 2011

TO: MEMBERS OF THE FINANCE COMMITTEE

- I. **SUBJECT:** Office of Audit Services Quarterly and Year-End Status Report
- II. **PROGRAM:** Audit Services
- III. **RECOMMENDATION:** Information Only
- IV. **ANALYSIS:**

In accordance with the Finance Committee's Audit Resolution Policy, the Office of Audit Services presents its Quarterly Status Report of audit activity. The following provides the status of projects and activities as of June 30, 2011.

1. Status of findings

Figure 1 - Current Fiscal Year Open Findings

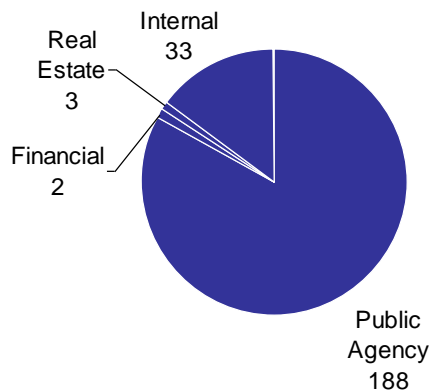
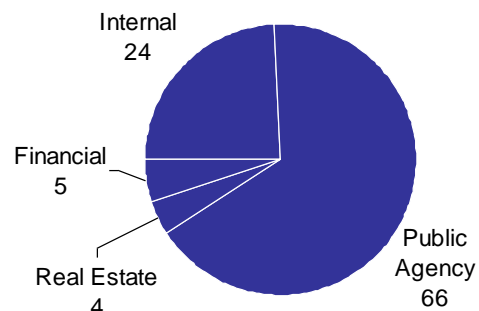


Figure 2 - Prior Fiscal Years Open Findings (2005-2010)



The charts above provide a summary of the types of open findings. Attachment 1A provides a dashboard status of the audit findings. Detail on all findings is available on file in the Office of Audit Services, upon request, and has been distributed to all appropriate divisions.

2. Acceptance of risk

In accordance with the Audit Resolution Policy, for findings unresolved for one year, the executive of the audited division is required to accept the risk of not implementing corrective action and to provide a written explanation as to why acceptance of risk is the most appropriate disposition of the issue.

As of June 30, 2011, there are 24 findings that were unresolved after one year. Attachment 2A provides the detailed status. The Office of Audit will work with executive management to obtain resolution of the finding or acceptance of risk. The specific findings over one year will be reported until resolved by implementation of the recommendation or acceptance of risk.

3. Finding trends

Current Year Fourth Quarter Findings

- There were 47 public agency findings issued during this fourth quarter and 20 findings, or 43 percent, have been addressed and are complete. Attachment 3A provides significant public agency review findings for this quarter.
- There were 16 internal audit findings issued during this fourth quarter. Attachment 4A provides an executive summary of the internal audits completed this quarter.

HIPAA-Related Findings

At the request of the Finance Committee, we have included the status of the Health Insurance Portability and Accountability Act (HIPAA) findings. All findings are now complete. The detailed status is provided in Attachment 5A of this agenda item.

Financial Statement Audit Findings

At the request of the Finance Committee, we have included the status of the two current year findings in Attachment 6A and the status of prior year findings in Attachment 6B of this agenda item.

Contracting Public Agency Reviews – common issues and examples:

- *Membership* (part-time employees were not enrolled into membership when eligibility requirements were met).
- *Automated Communications Exchange System* (Employer User Security Agreements were not on file and Delete ACES User Access forms were not submitted to CalPERS).
- *Incorrect reporting of compensation* (non-reportable compensation such as longevity pay, deferred compensation, shift overlap pay and on-call pay, and reportable compensation such as uniform allowance not reported).

Internal Audits – common issues and examples

- *Processes* (absent, incomplete, or outdated processes or implementation issues). Inadequate processes increase the risk of non-compliance with laws, regulations, and policy. Inadequate processes could also hinder achievement of business objectives.
- *Documentation* (absent, incomplete, or outdated documentation supporting transactions, reviews or contracts). Inadequate documentation increases the risk of ineffective program oversight and could also hinder succession planning efforts.

Real Estate Compliance Review – common issues and examples

- *Fees and unallowable costs* (charging for fees and costs not specified, correctly calculated, or allowable by agreement)
- *Vendor contracting* (improper bidding or unsubstantiated bids for work contracted, no executed contracts on file, or lack of required clauses)
- *Accounting and reporting* (weaknesses in accounting systems, inadequate reconciliations, untimely submission of reports)

4. Status of projects

Table A provides a summary of the projects by categories.

- Internal audit projects and consulting assignments focus on compliance, and the effectiveness and efficiency of CalPERS operations, systems, policies, and procedures. Internal audit also includes audits of health maintenance organizations contracting with the System, compliance audits of health care third-party administrators, and audits of external providers of investment-related services.
- Public Agency reviews include compliance reviews of employers belonging to the System.
- Financial statement and real estate audits are contract audits performed by external auditors.

Table A – Summary of Activities

Type of Project	2010-11 Audit Plan	Projects In Progress	Projects Complete
Internal Audit, Consulting and Follow-Up (Attachment 7A)	49 ^A	17 ^B	37 ^B
Public Agency Reviews (Attachment 7B)	48 ^A	40 ^B	56 ^B
Financial Statement and Real Estate Contract Audits (Attachment 7C)	n/a	5 ^B	9 ^B

^A - Includes seven deferred internal audits and three new projects for internal audits from 53 previously planned. For public agency, six deferred public agency reviews and a reduction of 25 reviews due to staff vacancies and reduced work hours from 79 previously planned.

^B - Includes audits started in prior fiscal year as shown in the Attachments.

5. Overview of Audit Services Staff Credentials

Education and Experience

Professional *Standard 1210* requires the internal audit activity to collectively possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities. Office of Audit Services staff possess proficiency in many areas that include internal controls, public agency compliance, risk assessment, financial audits, health programs, information technology systems, information technology security, investments, real estate, benefit administration, and project management. In addition, staff exhibit a high level of educational achievement, complemented with many years of CalPERS and total audit experience, as seen in Tables B through D below.

**Table B – Office of Audit Services
Audit Experience**

Office of Audit Services Experience (Years)	Staff
Up to Two	10
Three to Five	14
Six to Ten	12
More than 10	8

Table C – Total Years of Audit Experience

Total Audit Experience (Years)	Staff
Up to Two	3
Three to Five	13
Six to Ten	13
More than 10	15

Table D – Education

Education	Degrees
Associate of Arts	2
Bachelor of Arts or Science	38
Masters	7

Titles and Certifications

Audit Services staff, comprising the job titles shown below, in Table E and F, hold a wide variety of professional certifications.

Table E – Audit Services Job Titles

Title	No. of Staff
Chief Auditor	1
Assistant Division Chief	1
Supervising Management Auditors	2
Senior Program Evaluators	3
Senior Program Evaluator (Information Systems)	1
Staff Management Auditors	2
Information System Evaluators	4
Public Agency Evaluators	15
Internal Evaluators	<u>16</u>
Total Audit Positions	45

Table F – Professional Certifications

Certification	No. of Staff
Certified Internal Auditor	11
Certified Public Accountant	12
Certified Information Systems Auditor	3
Certified Governmental Financial Manager	3
Certified Investments and Derivatives Auditor	3
Certified Fraud Examiner	<u>1</u>
Total Certifications	33

6. Quality Assurance and Improvement Program

As part of our Quality Assurance and Improvement required by *Standard 1300*, the Office of Audit Services sends a customer satisfaction survey at the conclusion of internal audits and public agency reviews. The survey questions focus on the audit process and report, overall value, and communication. For 2010-11, the return response from internal management and public agencies was 28 and 15 percent, respectively. The results of the survey indicate internal management and public agencies' overall responses to the questions were generally positive.

Standard 1320 requires the Chief Auditor to communicate the results of the quality assurance and improvement program to senior management and the Board. As part of the Quality Assurance and Improvement Program, the Office of Audit Services performs internal assessments of the internal audit activity through ongoing reviews and periodic self-assessments. As a result of our self-assessment, the following three areas were identified that require corrective action, updating the Office of Audit Services Charter, updating our policies and procedures manual, and improving close-down procedures within our audit software program. We plan to target improvement in fiscal year 2011-12.

7. Definition of Internal Auditing, the Code of Ethics, and the *Standards*

Standard 1010 requires the Chief Auditor to discuss the definition of internal auditing, the Code of Ethics, and the *Standards* with senior management and the Board. The definition of internal auditing states the fundamental purpose, nature, and scope of internal auditing. The Code of Ethics states the principles and expectations governing the behavior of individuals and organizations in the conduct of internal auditing. It describes the minimum requirements for conduct, and behavioral expectations rather than specific activities. The *Standards* are mandatory and are principle-focused to provide a framework for performing and promoting internal auditing.

V. STRATEGIC PLAN:

This item is not a specific product of the strategic plan, but is required by the Finance Committee's Audit Resolution Policy and Procedures and the Office of Audit Services Charter.

VI. RESULTS/COSTS:

There is no additional cost for this specific agenda item.

MARGARET JUNKER, Chief
Office of Audit Services

PETER H. MIXON
General Counsel

Attachments